

Message Text

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ACTION ARA-10

INFO OCT-01 ISO-00 SP-02 USIA-06 AID-05 EB-08 NSC-05
TRSE-00 SS-15 STR-04 OMB-01 CEA-01 CIAE-00 COME-00
FRB-03 INR-07 NSAE-00 XMB-02 OPIC-03 LAB-04 SIL-01
L-03 H-01 PRS-01 PA-01 IGA-02 /086 W
-----041852Z 026083 /41

R 041740Z MAR 77

FM AMEMBASSY SAN JOSE
TO SECSTATE WASHDC 6625
INFO AMEMBASSY GUATEMALA
AMEMBASSY MANAGUA
AMEMBASSY PANAMA
AMEMBASSY SAN SALVADOR
AMEMBASSY TEGUCIGALPA

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GUATEMALA ALSO FOR ROCAP

E.O. &61652: N/A

TAGS: EFIN, ECON, CS

SUBJECT: FINANCE MINISTER DEFENDS 1977 GOVERNMENT BUDGET

1. SUMMARY. THIS MESSAGE DISCUSSES THE 25 PERCENT ANNUAL GROWTH OF GOVERNMENT SPENDING IN COSTA RICA OVER THE PAST TWO YEARS AND THE LARGE (24PERCENT-25PERCENT) BUDGETARY DEFICITS DURING THE SAME PERIODS RESULTANT CRITICISM FROM THE PRIVATE SECTOR; AND THE EXPLANATION OFFERED BY THE MINISTER OF FINANCE. THE EMBASSY OBSERVES THAT DESPITE THESE THEORETICALLY INFLATIONARY FACTORS, GOVERNMENT ECONOMIC POLICY HAS SUCCEEDED IN REDUCING THE RATE OF INFLATION FROM 38 PERCENT IN 1974, TO 14.3 PERCENT IN 1975, TO 9.2 PERCENT IN 1976. THIS ACCOMPLISHMENT SUGGESTS THAT A DEFICIT THE SIZE OF LAST YEAR'S IS MANAGEABLE BUT THE EMBASSY CONCLUDES THAT A LARGER DEFICIT, WHICH COULD OCCUR AS A RESULT

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OF POLITICAL PRESSURES IN A PRE-ELECTION YEAR, WOULD BE LIKELY TO RE-IGNITE INFLATION. END SUMMARY.

2. PERHAPS THE MOST CRITICAL POLITICAL/ECONOMIC ISSUE FACING COSTA RICAN POLICY MAKERS IN 1977 IS CENTRAL GOVERNMENT SPENDING. THE STATISTICS, VIEWED IN ISOLATION, ARE STRIKING: OVER THE LAST TWO YEARS

(1975 AND 1976) GOVERNMENT SPENDING HAS INCREASED AT AN ANNUAL RATE OF 251.034:3,5. 1977 EXPENDITURES SHOW A BUDGETED INCREASE OF 16 PERCENT OVER 1976 EXPENDITURES. FURTHERMORE, DEFICITS IN RECENT YEARS HAVE BEEN HIGH: \$82 MILLION OR 24 PERCENT OF THE BUDGET IN 1975; \$105 MILLION OR 25 PERCENT OF THE BUDGET IN 1976. THE 1977 DEFICIT HAS BEEN ESTIMATED AT \$129 MILLION OR 26 PERCENT OF THE AMOUNT BUDGETED.

3. THESE FIGURES HAVE ALARMED THE PRIVATE SECTOR. IN A HALF-PAGE NEWSPAPER AD, THE ASOCIACION NACIONAL DE FOMENTO ECONOMICO (ANFE), A CONSERVATIVE GROUP OF PROFESSIONALS AND BUSINESSMEN, POINTEDLY ASKED THE MINISTER OF ECONOMY TO ANSWER THE FOLLOWING QUESTIONS: HOW IS THE DEFICIT IN THE 1977 BUDGET TO BE FINANCED? ARE NEW TAXES PLANNED, AND, IF SO, WHAT ARE THEY? DO YOU BELIEVE THAT THE PRODUCTIVE SECTORS OF THE ECONOMY CAN SUPPORT NEW TAXES? THE COSTA RICAN CHAMBER OF COMMERCE, A LARGE AND POWERFUL ORGANIZATION, ENDORSED THE QUESTIONS POSED BY ANFE AND INVITED THE MINISTER OF FINANCE TO ANSWER THEM AT ONE OF THEIR MONTHLY LUNCHES.

4. IN HIS SPEECH TO THE LARGE GROUP OF CHAMBER MEMBERS THAT ATTENDED THE LUNCH, THE MINISTER OF FINANCE, PORFIRIO MORERA, ENDEAVORED TO EXPLAIN THE ROLE OF FISCAL POLICY WITHIN COSTA RICA'S GENERAL ECONOMIC POLICY. ACCORDING TO MORERA, HIGH GOVERNMENT BUDGETS AND DEFICITS DURING THE YEARS 1974, 1975 AND 1976 SHOULD NOT BE SEEN AS AN ISOLATED PHENOMENON BUT AS PART OF AN INTEGRATED APPLICATION OF BROAD ECONOMIC LIMITED OFFICIAL USE

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POLICY TO DEVELOPMENT GOALS. IN HIS OPINION, GOVERNMENT POLICY HAS BEEN EFFECTIVE IN OVERCOMING THE GRAVE PROBLEMS CAUSED BY THE RECESSION DURING 1974 AND 1975, AS WELL AS PROMOTING MORE EQUITABLE INCOME DISTRIBUTION.

5. MORERA ALSO DEFENDED THE HIGH DEFICITS IN RECENT YEARS BY POINTING OUT THAT THE HIGH RATES OF INFLATION EXPERIENCED DURING 1974 AND 1975 (23 PERCENT AND 21 PERCENT AS DZMEASURED BY THE GDP DEFLATOR) HAD A DIRECT IMPACT ON GOVERNMENT PURCHASES OF GOODS AND SERVICES FROM THE PRIVATE SECTOR. INFLATION ALSO BROUGHT ABOUT DEMANDS FOR HIGHER SALARIES FROM PUBLIC SECTOR EMPLOYEES. AT THE SAME TIME, THE RECESSION CAUSED A DROP IN GENERAL REVENUES AS BUSINESS ACTIVITY CONTRACTED, WHILE THE GOVERNMENT HAD TO SPEND MORE TO COUNTERACT THE RECESSION BY STIMULATING DEMAND IN THE ECONOMY.

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6. REFERRING TO THE SITUATION IN 1977, HE DEEMED THE HIGH BUDGET INEVITABLE AND THE LARGE DEFICIT MANAGEABLE. HE SAID THAT HE SHARES THE CONCERN OF THE ASSEMBLED CHAMBER, BUT THAT REDUCING THE BUDGET IS ALMOST IMPOSSIBLE DUE TO AUTOMATIC INCREASES IN THE EXPENDITURES OF APPROVED PROGRAMS AND OTHER LEGAL AND CONSTITUTIONAL OBLIGATIONS. HE DID ASSURE THE GROUP THAT THE GOVERNMENT WOULD ATTEMPT TO USE GOVERNMENT FUNDS MORE EFFICIENTLY. TO THIS END, HE SAID THAT A "COMMISSION TO REDUCE COSTS" HAS BEEN FORMED COMPOSED OF PEOPLE FROM THE MINISTRY OF FINANCE, THE MINISTRY OF THE PRESIDENCY, THE PLANNING OFFICE, THE CENTRAL BANK AND THE CIVIL SERVICE COMMISSION.

7. THE MINISTER ALSO EXPLAINED THAT IN HIS VIEW THE DEFICIT WAS "MANAGEABLE" BECAUSE IT COULD BE COVERED BY INTERNAL AND EXTERNAL BORROWING WITHOUT RECURRING TO MONETARY EXPANSION. HE ADDED THAT HIGH COFFEE
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EARNINGS IN 1977 WOULD FACILITATE SALES OF GOVERNMENT BONDS TO COSTA RICANS. MOREOVER, THE VENEZUELAN INVEST-

MENT FUND WOULD BE A PRIME SOURCE FOR THE MONEY NEEDED FROM ABROAD. HE DID NOT THINK THAT DEBT SERVICE PAYMENTS, CURRENTLY ABOUT 15 PERCENT OF THE BUDGET, WERE A BURDEN AT THIS POINT.

8. COMMENTS. WHILE THE RATE OF INCREASE IN GOVERNMENT SPENDING AND THE SIZE OF THE BUDGET DEFICIT IN RECENT YEARS LOOK ALARMING IN ISOLATION, THEY LOOK MUCH LESS SO IN THE CONTEXT OF THE OVERALL TREND OF THE ECONOMY. IT IS TRUE, AS MINISTER BARRERA STATED, THAT THE PRICES OF MANY GOODS AND SERVICES BOUGHT BY THE GOVERNMENT INCREASED SHARPLY OVER THE PAST SEVERAL YEARS. AS MANY OF THESE GOODS WERE IMPORTS, THE PRICE RISES COULD NOT BE BLAMED ON INFLATIONARY EFFECTS OF THE DEFICIT. IT SHOULD BE NOTED THAT THE COSTA RICAN GOVERNMENT SUCCEEDED IN REDUCING DOMESTIC INFLATION, AS MEASURED BY THE WHOLESALE PRICE INDEX, FROM 38 PERCENT IN 1974, TO 14.3 PERCENT IN 1975, TO 9.2 PERCENT IN 1976. BUDGETARY DEFICITS IN COSTA RICA DO NOT APPEAR TO HAVE A STRONG INFLATIONARY EFFECT BECAUSE: THE ECONOMY IS USUALLY OPERATING AT WELL BELOW CAPACITY; IT IS A VERY OPEN ECONOMY IN WHICH MUCH OF ANY INCREASE IN DEMAND IS SATISFIED BY IMPORTS; AND MANY CONSUMER GOODS ARE UNDER PRICE CONTROL.

9. IT WOULD APPEAR THAT A 1977 DEFICIT OF THE SAME MAGNITUDE AS LAST YEAR'S WOULD BE MANAGEABLE, BUT IF EXPENDITURES ARE ALLOWED TO GET OUT OF HAND IN THIS PRE-ELECTION YEAR AND RISE EVEN MORE THAN THEY HAVE OVER THE PAST TWO YEARS, THERE WILL BE A GRAVE DANGER OF RE-IGNITING INFLATION.

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Message Attributes

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